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Nos. 93 and 160

In the Supreme Court of the United States

OCTOBER TERM, 1930

NEW YORK LIFE INSURANCE COMPANY, PETITIONER

v.

FRANK COLLIS BOWERS, EXECUTOR OF THE ESTATE OF FRANK K. BOWERS, DECEASED, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK

FRANK COLLIS BOWERS, EXECUTOR OF THE ESTATE OF FRANK K. BOWERS, DECEASED, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK, PETITIONER

v.

NEW YORK LIFE INSURANCE COMPANY

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR FRANK COLLIS BOWERS, EXECUTOR

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OCTOBER TERM, 1930

No. 93

NEW YORK LIFE INSURANCE COMPANY, PETITIONER

v.

FRANK COLLIS BOWERS, EXECUTOR OF THE ESTATE OF Frank K. Bowers, Deceased, Formerly Collector of Internal Revenue for the Second District of the State of New York

No. 160

FRANK COLLIS BOWERS, EXECUTOR OF THE ESTATE OF Frank K. Bowers, Deceased, Formerly Collector of Internal Revenue for the Second District of the State of New York, petitioner

v.

NEW YORK LIFE INSURANCE COMPANY

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR FRANK COLLIS BOWERS, EXECUTOR

OPINIONS BELOW

The opinion of the District Court (R. 27-33) is reported in 34 F. (2d) 60. The opinion of the Cir-

cuit Court of Appeals (R. 184–191) is reported in 39 F. (2d) 556.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered March 10, 1930. (R. 192.) A petition for rehearing was filed by the Collector of Internal Revenue on March 20, 1930, and was denied on April 7, 1930. (R. 192.) Petitions for writs of certiorari were filed on April 26, 1930, in No. 93, and on May 26, 1930, in No. 160. (R. 194.) Writs of certiorari were granted on June 2, 1930. (R. 193.) Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

(1) Whether the Revenue Act of 1921 should be construed to repeal the provisions of Section 1000 (c) of the Revenue Act of 1918 so as to relieve life insurance companies from the payment of any capital stock taxes for the two years beginning July 1, 1920, and ending June 30, 1922, or for either of these years.

(2) Whether the Commissioner of Internal Revenue, in computing the basis for the capital stock tax of a mutual life insurance company for each of the four years beginning July 1, 1918, and ending June 30, 1922, erred in refusing to exclude the amounts shown in items 35, 36, and 37 of the company's statement to the Superintend-

ent of Insurance of the State of New York as of the end of the preceding calendar year, these items representing (1) dividends declared shortly after the end of that calendar year for payment to policyholders during the year in which they were declared and (2) an "Interim Accumulation Fund," which consisted of amounts set aside over a period of several years from which the company expected to declare dividends to holders of deferred-dividend policies in subsequent years.

STATUTES AND REGULATIONS INVOLVED

The statutes involved and also various regulations and rulings of the Treasury Department are printed in the appendices, pp. 59–92, *infra*. The Government contends that all of the taxes in question were properly collected under the following provisions of Section 1000 (c) of the Revenue Act of 1918:

> * * * The taxes imposed by this section shall apply to mutual insurance companies, and in the case of every such domestic company the tax shall be equivalent to $1 for each $1,000 of the excess over $5,000 of the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding accounting period used by such company for purposes of making its income-tax return: * * *

STATEMENT

The New York Life Insurance Company brought an action in the District Court against the Collector of Internal Revenue to recover capital stock taxes assessed against it and paid under the Revenue Act of 1918 for the four years beginning July 1, 1918, and ending June 30, 1922. (R. 1–18.) July trial was waived by written stipulation and the court adopted an agreed statement of facts as its findings. (R. 33–34.) The court concluded as a matter of law that the plaintiff was not entitled to recover anything on account of the amounts paid for the first three of these years, but held that the applicable statutes imposed no capital stock tax on life insurance companies for the year beginning July 1, 1921. It accordingly entered judgment for the plaintiff for the full amount claimed for that year, and dismissed the complaint as to the other years. (R. 35–36.) On appeals by both parties, the Circuit Court of Appeals affirmed the judgment. (R. 192.)

The company filed with the Collector of Internal Revenue, on forms prescribed by the Treasury Department for that purpose, returns for the years beginning on July 1, 1918, July 1, 1919, July 1, 1920, and July 1, 1921, for the special tax imposed by Section 1000, Title X, of the Revenue Act of 1918, ordinarily referred to as "Capital Stock Tax." These returns showed no such tax due from the company for any of these years. The Commis-

sioner of Internal Revenue assessed against the company capital stock taxes for each of these years for a substantial amount, varying from $124,500 for the year beginning July 1, 1918, to $94,134 for the year beginning July 1, 1921. The company paid the amounts assessed involuntarily and under protest, and duly filed claim for refund of all of these taxes, which claim was duly rejected. (R. 38–39.) The litigation involves two distinct questions—(1) for what years the applicable statutes imposed the tax on mutual life insurance companies, and (2) on what items the tax should be based. The answer to the first of these questions depends entirely upon the proper construction of certain statutory provisions and upon the effect of regulations and the practice of the Treasury Department. The second branch of the case involves another question of statutory construction and the application of the statute to certain items in the company's annual financial reports. To determine this matter, it is necessary to understand the nature of these items, and this requires consideration of the nature of the company's business and the procedure by which the items in question were determined by the company.

The Commissioner, in assessing capital stock taxes for each of the years in question, deducted from the book value of the taxpayer's "admitted assets" as of December 31 of the preceding year (1) the difference between the book value and the

market value of these "admitted assets"; (2) the amount of the legal reserves; (3) numerous other items known as "debt liabilities"; and (4) the statutory exemption of $5,000. The controversy is as to the propriety of the Commissioner's refusal to deduct from the book value of the company's "admitted assets" appearing in its statement to the Insurance Superintendent as of December 31 of the preceding year three items appearing in that statement under the schedule headed "V.—Liabilities, Surplus, and Other Funds," designated as follows:

> Item 35: Dividends declared on or apportioned to annual dividend policies payable to policyholders to and including December 31 [of the year following that for which the report was made], whether contingent upon payment of renewal premiums or otherwise.
>
> Item 36: Dividends declared on or apportioned to deferred dividend policies payable to policies to and including December 31 [of the year following that for which the report was made].
>
> Item 37: Amount set apart, apportioned, provisionally ascertained, calculated, declared or held awaiting apportionment upon deferred dividend policies not included in Item 36.

In each year the aggregate of these three items more than exceeded the sum upon which the Commissioner assessed a capital stock tax, and if these items should have been excluded the company was

liable for no capital-stock tax for any of the years in question. The amount of Item 35 varied from $12,437,514, shown on the annual report as of December 31, 1917, to $16,431,339, shown on the annual report as of December 31, 1920; the amount of Item 36 varied from $14,123,549.64, shown on the report of December 31, 1917, to $21,015,315.87, shown on the report of December 31, 1920; and the amount of Item 37 varied from $107,041,778, shown on the report of December 31, 1917, to $76,176,646 shown on the report of December 31, 1920. (R. 46–58.)

The agreed statement of facts (which the District Court adopted as its findings) (R. 37–173) contains a detailed explanation of the company's manner of carrying on business, as well as a recital of other vital facts, and includes as exhibits copies of certain resolutions of the company's Board of Directors and copies of the annual statements filed by the company in the office of the Superintendent of Insurance of the State of New York for the calendar years ending December 31, 1916, December 31, 1917, December 31, 1918, December 31, 1919, and December 31, 1920. The following is an epitome of the most essential facts found.

The company is a corporation incorporated by special charter under the laws of New York and transacted the business of life insurance on a purely mutual, level premium plan. It never has had any capital stock or stockholders, and its business is

managed by a Board of Directors elected by the policyholders and officers appointed by that Board. (R. 37.) It is the essence of mutual life insurance upon this plan that each policyholder is entitled to receive his insurance at cost. The company collects level premiums in advance. The premium consists of the sum which it is calculated that each insured must pay so as to put the company in funds with which to pay all outstanding policies as they become due, plus a sum, technically called "loading", to take care of expenses, unforeseen contingencies, and the like. (R. 39–40.)

The company issued contracts on two general plans, one known as the "annual-dividend plan" and the other as the "deferred-dividend plan." The annual-dividend plan provides for accounting to the insured each year on the anniversary of his policy for annually ascertained divisible surplus for the prior year or years. In its deferred-dividend policies, the company agreed at a designated period after the time when the insurance took effect to account to the policyholders for the amount of the annually ascertained divisible surplus plus accumulated interest and plus a proportionate share of the accumulated overpayments of all policyholders of the class whose several policies were not in force at the time named therein for paying a dividend. A deferred dividend policyholder lost or forfeited all share in this fund by the lapse of his policy or by his death before the divi-

dend date named therein, in which event the amount to which he would have become entitled remained in the fund to be distributed among the surviving members whose policies were in force on maturity of the same in the year in which the dividend became payable. (R. 42–45.)

The company's charter and the laws of New York provided that as soon as practicable after December 31 of each year it should cause a statement to be made of its affairs, ascertain the surplus earned by it during the year, and determine the amount of surplus for the current and prior years which might, in the judgment of the Board of Directors, safely be distributed. In January or February of each year the company took such action. The first step in this determination was to ascertain the total receipts for the year in question, which was the sum of all premiums received during the year plus receipts from other sources. The company then ascertained the amount of policy claims paid for such year, the amount of its current expenses for such year, and the several sums required to increase its reserves. The total of these amounts was subtracted from the total receipts, and the difference was designated as the "Surplus" for the year. The Board of Directors at its meeting transferred to an account called "Undivided Surplus Account" not only this surplus for the year but also a certain amount from the item designated "Latent Fund for Contingencies and Dividends." (Neither the "Undivided

Surplus" nor the "Latent Fund" appear in the annual statements to the Insurance Superintendent.) At the same meeting the board appropriated from the "Undivided Surplus Account" a certain amount as dividends to those policies participating annually in surplus on their anniversaries in the current year, i. e., the year in which the appropriation was made. The sum so appropriated each year was shown as Item 35 in the annual statement as of the end of the preceding year. (R. 40–41, 47, 62.)

Part of this "Undivided Surplus Account" was each year credited to the "Interim Accumulation Fund." This last named fund was held by the company awaiting apportionment among its deferred dividend policyholders on the several dates named in their respective policies for paying such dividend. Thus each year this fund, which had been accumulating for many years, was added to, and each year a certain amount was appropriated from it for the payment of dividends to the deferred dividend policyholders whose policies were to mature in the current year. The amount so appropriated shortly after the end of the calendar year constituted "Item 36" in the annual statement as of the end of the calendar year which ended just before the appropriation. (R. 42, 48.)

The balance in this "Interim Accumulation Fund" was held by the company awaiting apportionment among the deferred-dividend policyhold-

ers in subsequent years. The amount held in the "Interim Accumulation Fund," as affected by adjustments due to the addition to and subtractions from it shortly after the end of the year, appeared in the annual statement as "Item 37." (R. 42, 49.)

The "Undivided Surplus Account" evidently existed only for purposes of the meeting of the Board of Directors, as the entire amount of it was credited at that meeting to some other account. The balance which remained in it after the appropriations above described was transferred to the "Security Fluctuation and General Contingency Fund," except in one year. At the meeting of February 13, 1919, a transfer was made from the "Security Fluctuation Fund" to the "Undivided Surplus Fund," instead of from the "Undivided Surplus Fund" to the "Security Fluctuation Fund." (R. 61–74.)

The company's assets are in no wise segregated or in any way ear-marked for investment purposes, and the company did not separately invest any sums shown in Items 35, 36, and 37. When, as in Item 37, a specified sum was held to the credit of a group or where a sum was held to the credit of a single individual, the company each year at the annual accounting increased the sum so held, with interest at the average rate earned during the preceding year on all of its invested funds. (R. 60.)

The company made its income tax returns on the cash basis for each calendar year. (R. 59–60.)

In the annual statements to the Insurance Superintendent the company's "admitted assets" (which the Commissioner used as a starting point in computing the assessment of the tax) included certain sums which had accrued but had not been received, and the items which were subtracted as liabilities included certain liabilities which had accrued but had not been paid. (Cf. R. 46 with R. 107–114.)

SPECIFICATION OF ERRORS TO BE URGED

On the phase of the case as to which the taxpayer prevailed in the court below, we contend that the Circuit Court of Appeals erred:

1. In holding that the income tax imposed upon life insurance companies by Section 243 of the Revenue Act of 1921 was in lieu of the capital stock tax imposed upon such companies by Section 1000 (c) of the Revenue Act of 1918 for the period beginning July 1, 1921, and ending June 30, 1922.

2. In holding that respondent was entitled to recover the capital stock tax paid for the period beginning July 1, 1921, and ending June 30, 1922.

SUMMARY OF ARGUMENT

I

The taxpayer is liable for capital stock taxes for four years beginning July 1, 1918, and ending June 30, 1922. It contends that the applicable Revenue Acts imposed no capital stock tax on life insurance companies for the two years be-

ginning July 1, 1920, and July 1, 1921, respectively. Each of the courts below held that a tax was imposed for the first of these periods, but was not imposed for the last of them. We maintain that it was imposed for both of these periods.

The decision of the District Court was based upon its assumption that the tax collected under the fourth assessment, i. e., for the year July 1, 1921, through June 30, 1922, "would have become due only on July 1, 1922." We submit that this was error, and that under the Revenue Act of 1918 the capital stock taxes were payable on or shortly after July 1 of each of the years 1918, 1919, 1920, and 1921, in advance for the period of a year beginning on July 1. The first capital stock taxes were imposed by Section 407 of the Revenue Act of 1916, and the practice of the Treasury Department under this was to require returns to be filed each July and to require the tax to be paid then for the ensuing fiscal year. The Revenue Act of 1918, which was approved February 24, 1919, repealed the capital stock tax provisions of the Revenue Act of 1916. Section 1000 of the 1918 Act imposed the tax involved in the instant case "on and after July 1, 1918, in lieu of the tax imposed by the first subdivision of Section 407 of the Revenue Act of 1916." The regulations and practice under the new Act treated the tax as payable in advance for the period of a year beginning July 1. The forms of the Treasury Department so provided and the taxpayer made

its returns on these forms. There is clear indication in *Hecht* v. *Malley*, 265 U. S. 144, 163–164, that the tax was payable in advance.

Consequently, on July 1, 1921, before the passage of the 1921 Act, the taxpayer came under an absolute liability to pay the capital stock tax for the privilege of carrying on its business for the ensuing year. The Circuit Court of Appeals recognized this, but held that the 1921 Act operated to relieve the taxpayer of liability for this tax. But we submit that there is no intimation in the 1921 Act, passed November 23, 1921, that Congress intended to remit the capital stock taxes which had already become due and payable. Section 1400 (a) of the 1921 Act provided for the repeals of various parts of the Revenue Act of 1918 to take effect at certain different designated dates. The repeal of Title X, which included the capital stock tax, was to take effect on January 1, 1922, and the repeal of certain other parts of the Act of 1918, including the income tax provisions and the profits tax provisions, was as of January 1, 1921. The postponement of the repeal of the capital stock tax until January 1, 1922, is so specific that it can not be disregarded, particularly in the light of Section 1400 (b), which provides:

> The parts of the Revenue Act of 1918 which are repealed by this Act shall (unless otherwise specifically provided in this Act) remain in force for the assessment and collection of all taxes which have accrued

under the Revenue Act of 1918 at the time such part ceased to be in effect.

We maintain that the other provisions of the Act of 1921 on which the taxpayer and the Circuit Court of Appeals relied were not intended to nullify these express provisions.

The construction for which we contend effects an orderly program and does not compel a life insurance company to pay in any one year more taxes than Congress intended it to pay annually. The construction adopted by the Circuit Court of Appeals would allow life insurance companies in 1921 to escape part of the taxes to which they were subject in prior years without paying any part of the taxes to which they were subject in later years.

II

The Commissioner acted correctly in refusing to deduct from the assets on which the capital stock tax was based in each year the amounts shown in Items 35, 36, and 37 of the annual statement to the Insurance Superintendent as of December 31 of the preceding year.

Section 1000 (c) of the Revenue Act of 1918 imposed on every domestic mutual insurance company a tax based upon "the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding

accounting period used by such company for purposes of making its income tax return." The company made its income tax return on the basis of the calendar year. The return for capital stock tax purposes was prepared each year in July (or later) for a year beginning July 1.

We maintain that all of the three items in question were "surplus" within the meaning of the statute. Whether the words in the statute "maintained for the general use of the business" modify the word "surplus" is unimportant, as surplus is, of course, maintained for the general use of the business, inasmuch as it is employed in financial operations and is available to meet obligations. The word "surplus" must include so much of the assets of a mutual life insurance company as remain after deducting the amount of all existing matured claims and the legal reserve for payment of insurance which will mature in the future.

In a mutual company, the policyholders are associates in the business as to which they are investors, as well as creditors of the group as a whole. They are, therefore, the collective owners of all profits which the company makes, and these profits are distributed among them in the form of dividends. The profits arise to a great extent from investment of funds and, to a smaller extent, from redundancy in premiums paid by the policyholders. Their rights to dividends and to control over the assets of the corporation are similar to the rights

of stockholders in a stock corporation. While each policy provides for the declaration of the profits in the form of dividends, it is as a charter—also a contract—provides for the declaration of dividends to shareholders in a stock company.

The items in question were nothing but bookkeeping items and existed as separate funds only on the books of the company. The company's assets were in no way segregated or in any way earmarked for investment purposes, and the company did not separately invest any sums shown in the items in question. At the end of the year for which the statement to the Insurance Superintendent was made, no person had any right to any particular amount on account of any of the three items. Although the company's charter, the policies, and the New York insurance law all required the directors to make appropriations for dividends shortly after the end of each year if circumstances warranted so doing, the amount of dividends to be declared was left largely to the discretion of the directors, and we are aware of no case in which it has been held that the directors could be forced to declare a dividend different from what they actually did declare. None of these items constituted trust funds, and it has been held by the highest court of New York that even upon the maturity of his policy a policyholder has no right to require an accounting of the funds of the company in the absence of a proof of wrongdoing or mistake.

The creation of the "Interim Accumulation Fund," Item 37, had no legal effect. It was maintained merely to show the result of the calculations and determinations of the directors and officers of the company over a period of years. If unforeseen events should occur, the amount represented by this item could, if necessary, have been devoted to the payment of life insurance on policies which matured unexpectedly, as well as of other valid claims against the company. The same is true, we submit, of Items 35 and 36, i. e., the amount of the dividends, at the end of the year before the dividends were declared. Not until the dividends were declared could any policyholder maintain an action to recover the dividend if the company had refused to pay it.

Consequently, the amounts represented in Items 35 and 36 up to the time of the declaration of the dividend and the amounts represented in Item 37 at all times were subject to no different obligations than they would have been subject had they been carried in a single account entitled simply "Surplus." The amount added each year to the "Interim Accumulation Fund," as well as the amount declared as a dividend payable to holders of annual dividend policies, passed through an account known as "Undivided Surplus Account." This account was composed partly of the profits for the year, which are designated in the company's charter, in the resolutions of the directors, in the poli-

cies, and also in the agreed statement of facts as "Surplus" or "Divisible Surplus." The rest of the "Undivided Surplus Account" was composed of appropriations made from the "Latent Fund for Contingencies and Dividends" and from the "Security Fluctuation and General Contingency Fund." This Court has designated the funds which went into the items now under consideration as "surplus." *New York Lift Ins. Co.* v. *Edwards*, 271 U. S. 109, 115. All of these funds alike were subject to distribution to policyholders proportionately to such extent as the directors felt it safe to diminish these funds.

The tax should be measured by business and financial realities and not by bookkeeping forms or mere names. *Hecht* v. *Malley*, 265 U. S. 144, 163. The Treasury Department has always construed Section 1000 as requiring the inclusion of the three items in question, and it has also allowed the taxpayer the benefit of including the items in question as surplus in computing invested capital for purposes of the profits tax.

If the items in question do not come within the description of "surplus or contingent reserves maintained for general use of the business," Item 37, at least, comes within the description "any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding accounting period used by such company for purposes of making its income tax return." The word "reserves" in this

statute can not be restricted to its technical meaning because there are no reserves in the strict sense which come within this description. Item 37, known as the "Interim Accumulation Fund," was designated in the resolutions adopted by the directors as a "reserve." The additions to it were included in net income under the provisions of Title II, relating to the income tax.

The items in question are not excluded by Section 1000 (b). The placement of the provisions of Section 1000 (c), relating to mutual insurance companies, shows that (b) is not intended to limit (c), and the legislative history of the Act shows that (b) relates only to stock companies.

ARGUMENT

I

THE TAXPAYER IS LIABLE FOR CAPITAL STOCK TAXES FOR FOUR YEARS BEGINNING JULY 1, 1918, AND ENDING JUNE 30, 1922

The taxpayer contends that in any event the applicable Revenue Acts imposed no capital stock tax on life insurance companies for the two years beginning July 1, 1920, and July 1, 1921, respectively. Each of the courts below held that a tax was imposed for the first of these periods, but was not imposed for the last of them. We maintain that it was imposed for both of these periods, as well as for the two years beginning July 1, 1918, and July 1, 1919.

The decision of the District Court was based upon its assumption that the tax collected under the fourth assessment, i. e., for the year July 1, 1921, through June 30, 1922, "would have become due only on July 1, 1922." (R. 32.)

The Circuit Court of Appeals, although realizing that the tax was payable in advance, nevertheless held that the statute was repealed so as not to be in effect for this fourth year. (R. 190.)

We submit that both courts erred.

(A) Under the Revenue Act of 1918, the capital stock taxes were payable on or shortly after July 1 of each of the years 1918, 1919, 1920, and 1921, in advance for the period of a year beginning on July 1.

The first capital stock taxes were imposed by Section 407 of the Revenue Act of 1916,[1] which was approved September 8, 1916. It imposed these taxes "on and after January 1, 1917." These were designated as "special taxes" in the Revenue Act of 1916. Inasmuch as the Act of October 1, 1890,[2] provided that "all special taxes shall become due on the first day of July," and it had been the practice to require payment in advance, and Sec. 409 of the 1916 Act made such administrative provisions a part of the 1916 Act, the Treasury Department, in Article 3 of Regulations 38,[3] promulgated October 19, 1916, under the Revenue Act of 1916, stipulated that—

> the capital stock tax, therefore, which becomes effective January 1, 1917, will be payable in January, 1917, on returns to be made during that month for the six months ending June 30, 1917. In July, 1917, and annually in July thereafter returns must again be made and the tax paid for the ensuing fiscal year.

This principle was followed in the form of return prepared by the Treasury Department. Thus,

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[1] This is printed on p. 59, *infra*.

[2] See p. 66, *infra*.

[3] This is printed in full on pp. 75–76, *infra*.

the form to be made out in July, 1918, contained the following words on the heading: [4]

> Return of Fair Value of Capital Stock for the Fiscal Year ended June 30, 1918.
> Tax Payable in Advance for the Year ending June 30, 1919.

And the instructions printed on this form included the following: [5]

> 1. *Nature of tax.*—The capital stock tax due July 1, 1918, is an excise tax payable in advance for the privilege of doing business from July 1, 1918, to June 30, 1919. The amount of the tax is payable to the collector at any time after July 1, 1918, but penalties for nonpayment do not attach until 10 days after notice and demand has been served by the collector upon the taxpayer.
>
> 2. *Date of filing returns.*—On or before July 31, 1918, and annually thereafter during the month of July.

The Revenue Act of 1918, which was approved February 24, 1919, repealed Title IV of the Revenue Act of 1916 (of which Section 407 was a part). See § 1400(a). Section 1000 (under Title X—"Special Taxes") of the Revenue Act of 1918 imposed the tax involved in the instant case "on and after July 1, 1918, in lieu of the tax imposed by the first subdivision of section 407 of the

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[4] For facsimile of this Form 707, see Regulations 38 (Revised), in Volume 20, Treasury Decisions, Internal Revenue, at page 470.

[5] 20 Treasury Decisions, Internal Revenue, p. 476.

Revenue Act of 1916." Section 1305 extended generally the existing administrative provisions of law, and under date of April 29, 1919, the Treasury Department promulgated "Regulations 50, relating to the capital stock tax under the Revenue Act of 1918," Article 1 of which provided:

> The tax became effective as of July 1, 1918, and is to be paid annually in advance for each year beginning July 1, in lieu of the capital-stock tax imposed by the Revenue Act of 1916. The tax for the first year ending June 30, 1919, although necessarily not payable in advance, must be paid upon notice and demand by the collector. * * *

Form 707, which had been used under the 1916 Act, was revised from time to time while the 1918 Act was in effect, but it always clearly indicated that the tax was payable in advance.*

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* Thus the form, as revised February, 1921, for use in that year was headed:

1922 RETURN

CAPITAL STOCK TAX

Return for Domestic Corporations

(Sec. 1000, Title X, Revenue Act of 1918)

File with Collector of Internal Revenue for your district on or before July 31, 1921, to avoid penalty

* * * * * *

TAX PAYABLE ANNUALLY IN ADVANCE

Return for taxable period July 1, 1921, to June 30, 1922, based on fair average value of capital stock for preceding year

CAREFULLY READ ALL INSTRUCTIONS BEFORE MAKING RETURN

The instructions on the return included the following:

1. *Nature of tax.*—The capital stock tax due July 1, 1921, is an excise tax payable in advance for the privilege of doing business from July 1, 1921, to June 30, 1922.

2. *Date of filing returns.*—During the month of July and annually thereafter.

It is, therefore, clear that at all times the Treasury Department treated capital stock taxes as payable in advance for the period of a year beginning July 1.[7] As this practice had been in effect under the Revenue Act of 1916, Congress, by the Act of 1918, obviously intended to continue this practice, and the language of Section 1,000 itself indicates that it intended to impose the new tax for the year beginning July 1, 1918.[8]

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[7] Article 2 of Regulations 64 (*infra*, p. 79), promulgated under the 1921 Act, made the same provision in regard to the capital stock tax under that Act. The same provision was also made by Article 2 of Regulations 64 (1924 ed.), promulgated under the 1924 Act.

[8] Section 1000 of the Revenue Act of 1921 (pp. 63–64, *infra*) and Section 700 of the Revenue Act of 1924 imposed capital stock taxes, in lieu of those previously imposed, "on and after July 1, 1922," and "on and after July 1, 1924," respectively. With the administrative procedure before it, Congress not only did not interfere with it, but reenacted capital stock tax provisions in such a way as to manifest approval of the administrative procedure. See *National Lead Co.* v. *United States*, 252 U. S. 140, 145–146; *Brewster* v. *Gage*, 280 U. S. 327, 336. Additional evidence that Congress intended the special taxes to be paid in advance is found in the fact that each of the Revenue Acts provided that any person "who carries on any business or occupation for which a special tax is imposed * * * without having paid the special tax therein provided, shall, besides being liable to

In *Hecht* v. *Malley,* 265 U. S. 144, 163–164, this Court said, in regard to the capital stock tax, that the Act of 1918 "was retroactive in its provisions and covered the year ending June 30, 1919." It seems that it would not have been necessary for the Court to have considered this matter if the tax were not due and payable at the beginning of the year in July, 1918. Otherwise, the tax would have been imposed for the year in question even if the Act had not been retroactive.

We conclude that, before the Revenue Act of 1921 was approved on November 23, 1921, returns had been required[9] for capital stock taxes and capital stock taxes had become due and payable under the 1918 Act for four different years, i. e., the years beginning July 1 of 1918, 1919, 1920, and 1921.

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the payment of such special tax" be subject to a certain penalty or to imprisonment. See Section 408 of the Revenue Act of 1916, Section 1005 of the Revenue Act of 1918, Section 1004 of the Revenue Act of 1921, Section 704 of the Revenue Act of 1924. The capital stock taxes were repealed by Section 1200 of the Revenue Act of 1926 as of June 30, 1926, and there have since been no such taxes in effect.

[9] Although the record does not contain copies of the returns made by the taxpayer under the capital stock provisions of the Act of 1918 and the findings do not state on what date such returns were made, it appears both from the findings and from the complaint that the taxpayer filed a return on the form furnished by the Treasury Department for each of the four years beginning July 1, 1918, and ending June 30, 1922. (R. 2, 38.) Its complaint asserted four causes of action, each being for the tax paid for one year, the first being headed, "For the recovery of the capital stock tax paid for the period ending June 30th, 1919," and the fourth (as to which the courts below allowed recovery) being "for the period ending June 30th, 1922." (R. 15.)

Therefore, the basis falls for that part of the decision of the District Court which is adverse to us.[10]

(B) The Revenue Act of 1921 did not remit the capital stock tax which had become due in July, 1921

It is clear that on July 1, 1921, before the passage of the 1921 Act, the taxpayer came under an abso-

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[10] The Circuit Court of Appeals answered the reasoning of the District Court on this point in the following effective manner (R. 191):

"* * * It is true, as the district court observed, that § 1000 (c) of 1916 provides that 'the taxes imposed * * * shall not apply in any year to any corporation which was not engaged in business * * * during the preceding year'; and § 1000 (a) (1) computes them on 'the fair average value' of the capital for the preceding year. Of course it is impossible to calculate such a tax in the case of a company that had done no business during any part whatever of the preceding year. But § 1000 (c) does not say that the company must have been in business 'during the whole of the preceding year,' but only 'during the preceding year.' The same applies to the use as a basis of the 'fair average value—for the preceding year.' It was entirely possible to compute the tax in the case of a company which had been in business for a part of the preceding year, and this satisfies all that the words demand. The Court of Claims (*Washington Water Power Co.* v. *U. S.*, 56 Ct. Claims 76), has decided in a case arising under the Act of 1916, that the tax is payable in advance, and this seems to us the proper construction. Finally, as we have said, the tax had its origin in the Revenue Act of 1916, which imposed it for the year beginning January 1, 1917. While it is possible that Congress meant to levy it for a period during which the act was not in effect, the language is 'on and after January 1, 1917.' It is more likely that such an excise in accordance with the usual theory, was laid prospectively upon an activity to be engaged in, than upon its pursuit during a time when there was no tax in view."

lute liability to pay a tax for the privilege of carrying on its business for the ensuing year. There is no intimation in the 1921 Act, passed November 23, 1921, that Congress intended to remit the tax which had already become due and payable.

Section 1400 (a) of the Act of 1921 [11] provided for repeals of various parts of the Revenue Act of 1918, to take effect at certain different designated dates. The repeal of Title X, which included the capital stock tax, was to take effect on January 1, 1922, and the repeal of certain other parts of the Act of 1918, including the income tax provisions and the profits tax provisions, was as of January 1, 1921. The postponement of the repeal of the capital stock tax until January 1, 1922, is so specific that it can not be disregarded, particularly in the light of Section 1400 (b), which provides:

> The parts of the Revenue Act of 1918 which are repealed by this Act shall (unless otherwise specifically provided in this Act) remain in force for the assessment and collection of all taxes which have accrued under the Revenue Act of 1918 at the time such parts cease to be in effect * * *.

The construction contended for by the taxpayer and that adopted by the Circuit Court of Appeals would give no effect whatever to these provisions as applied to this tax.

We submit that the other provisions of the Act of 1921 on which the taxpayer and the Circuit

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[11] Printed on pp. 64–65, *infra*.

Court of Appeals relied were not intended to nullify the express provision of Section 1400 quoted above. That court based its conclusion chiefly upon another sentence in Section 1400 (b) which reads as follows:

> In the case of any tax imposed by any part of the Revenue Act of 1918 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act.

This sentence, we submit, does not operate to accelerate the repeal provided for in Section 1400 (a), as held by the Circuit Court of Appeals, but merely to extend the provisions of the Revenue Act of 1918 beyond the time of its repeal under certain circumstances. Moreover, the "corresponding tax" under the 1921 Act did not take effect until July 1, 1922, for Section 1000 (a) of the Revenue Act of 1921 provided that—

> * * * on and after July 1, 1922, in lieu of the tax imposed by section 1000 of the Revenue Act of 1918—

certain excise taxes should be imposed.

It was the evident intent of Congress to continue the capital stock tax imposed by the Revenue Act of 1918 without interruption until the capital stock tax imposed by the Revenue Act of 1921 became effective on July 1, 1922. But the capital stock tax imposed by the 1921 Act was not applicable to life

insurance companies. In lieu thereof such companies were subjected to a special income tax by Section 243. This was in lieu of the new capital stock tax and there is no evidence of an intent that the 1918 capital stock tax was to end any earlier in the case of life insurance companies than in the case of other companies. On the contrary, the legislative history indicates that Congress intended life insurance companies to remain subject to the 1918 capital stock tax until all companies were relieved from it by the incidence of the new tax.

The report of the Senate Finance Committee (Senate Report No. 275, 67th Congress, 1st Session) accompanying the Revenue Bill of 1921, contains the following (p. 20):

> Sections 242–246 provide a new plan for the taxation of life insurance companies, substantially similar to the plan embodied in the revenue act of 1918 as first adopted by the Senate. * * * The new tax would take the place of the present income and excess-profits taxes for the year 1921, *and life insurance companies would share with other insurance companies in the repeal in the year 1922 of the capital-stock tax* and the taxes imposed by section 503. The new tax will yield a larger revenue than the taxes which it is proposed to replace. (Italics supplied.)

In the same Report (p. 30), the Senate Finance Committee said:

Section 1000 provides for the repeal of the capital-stock tax imposed by section 1000 of the revenue act of 1918 after June 30, 1922.

The brief for the taxpayer stresses the fact that Section 263 of the 1921 Act provides that the income tax provisions (including Section 243, which imposes the income tax on life insurance companies in lieu of the other taxes imposed by the Revenue Act of 1921) "shall take effect as of January 1, 1921." But this provision operated merely to require that the taxes on account of 1921 income should be computed in accordance with the new provisions. The Act of 1921 did not impose any new tax which was payable in 1921,[12] but provided that during that year the taxes which had accrued under the 1918 Act should be paid. See Sections 200, 230, 241, 227, and 250 of the Act of 1921, as well as the provisions of Section 1400 (b), quoted on p. 28, *supra*.

The taxpayer's brief also argues that the capital stock tax due in 1921, imposed by the 1918 Act, was repealed by implication by the Act of 1921. This argument is based upon the contention that

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[12] Except as to corporations making their returns upon the basis of a fiscal year other than the calendar year. Such corporations were taxed under the 1918 Act on so much of the income for the fiscal year as was attributable to 1920 and under the 1921 Act on so much of the income as was attributable to 1921. See Section 205 of the 1921 Act, and p. 36, *infra*.

the Act of 1921 "covers the whole field embraced by the Act of 1918." But the question is how the two Acts dovetail together, and at what time the provisions of the Act of 1921 replace those of the Act of 1918. In view of the explicit statements in the Act of 1921 that the repeal of the capital stock tax is as of January 1, 1922, that the new capital stock tax is not to take effect until July 1, 1922, and that taxes which have accrued prior to the passage of the Act of 1921 shall not be affected, there is no room for any implication. Under the provisions of Section 13 of the Revised Statutes (p. 66, *infra*), "liabilities incurred" under a repealed statute are preserved unless the repealing Act expressly or by necessary implication excludes the operation of that section, the provisions of which are to be treated as if incorporated in and as a part of subsequent enactments. *Hertz* v. *Woodman*, 218 U. S. 205, 217–218; *Page* v. *Skinner*, 293 Fed. 468, 470 (D. Colo.), affirmed, 298 Fed. 731 (C. C. A. 8th), certiorari denied, 266 U. S. 625.

In holding that Congress did not intend that life insurance companies should be subject to the 1918 capital stock tax at a time when the new income tax imposed by Section 243 of the 1921 Act was in effect, the Circuit Court of Appeals has overlooked the fact that life insurance companies were specifically subjected by the 1918 Act to four different taxes at the same time. Section 230 of that Act imposed an income tax, Section 301 imposed an excess profits

tax, Section 503 imposed a tax on the issuance of insurance policies, and Section 1000 imposed a capital stock tax.

By its terms, Section 243 of the 1921 Act imposed taxes in lieu of Section 1000 of the same Act and also in lieu of taxes imposed by Section 230 and by Title III of that Act; but it did not impose any tax in lieu of the taxes here in question imposed by Section 1000 of the 1918 Act. One must therefore look to the corresponding Section 1000 of the 1921 Act to find provision for the imposition of any tax which takes the place of the taxes previously imposed by Section 1000 of the 1918 Act. But Section 1000 of the 1921 Act is by its terms effective for this purpose only on and after July 1, 1922. Thus Section 243 imposed no taxes in lieu of those capital stock taxes which became due and payable prior to July 1, 1922. As by its terms that section imposed no tax in lieu of the tax here in question, Section 1400 (b) of the 1921 Act continued the provisions of Section 1000 of the 1918 Act in force until July 1, 1922, when the corresponding tax under the 1921 Act (i. e., the tax imposed by Section 1000 of that Act) took effect.

It is only when we are asked if an insurance company is required to pay a capital stock tax under the Revenue Act of 1921 (that is, for the year beginning July 1, 1922—a year following the last year taxed in this case) that we consider whether Section 1000 (b) exempting certain insurance cor-

porations from this tax applies. Whether it is then to be exempted depends upon a consideration of the income tax provisions of the 1921 Act and not of any earlier Act. If under the 1921 Act an insurance company paid certain income tax in lieu of all other taxes, then it is exempt from the payment of a capital stock tax under the 1921 Act. This, of course, can have no reference to its tax liability under the 1918 Act. The Government is not seeking to impose or to uphold a tax for the year beginning July 1, 1922.

The construction for which we contend effects an orderly program and does not compel the taxpayer to pay in any one year more taxes than Congress intended it to pay annually. Under our construction a life insurance company like the taxpayer here would pay the following taxes in the year 1921: (1) the income tax imposed by the 1918 Act on income for the calendar year 1920; (2) profits tax [18] imposed by the Act of 1918 on income for the year 1920; (3) the capital stock tax imposed by the Act of 1918, payable July 1, 1921, for the year beginning on that date; and (4) the tax on issuance of policies. Thus, during 1921 the taxpayer would pay only those taxes provided under

[18] In view of the holding in *Duffy* v. *Mutual Benefit Co.*, 272 U. S. 613, probably many mutual companies actually paid no profits tax.

the Act of 1918. In the year 1922 it would pay only the tax imposed by the Act of 1921 on income for the year 1921. There consequently is no duplication or overlapping, and it is apparent that the provisions for repeal in the Act of 1921 were not drawn carelessly or inadvertently but that they were designed and were well calculated to dovetail the two Acts.

On the other hand, the construction adopted by the Circuit Court of Appeals would produce the following result: During the year 1921 the taxpayer would pay only (1) income tax on income for the year 1920 under the Act of 1918, and (2) profits tax for the year 1920 under the Act of 1918; and it would pay no capital stock tax whatever and it would pay nothing on account of the larger income tax imposed by the Act of 1921, which was first payable in the year 1922. And in the year 1922 it would pay only that tax. The result of the decision of the Circuit Court of Appeals consequently is to allow the taxpayer in 1921 to escape part of the taxes to which it was subject in prior years without paying any of the taxes to which it was subject in later years.

Congress was obviously concerned with the amount of revenue which would be collected in each calendar year and with the amount which the taxpayer would actually pay in any calendar year, rather than the amount of taxes which might accrue in the case of any taxpayer during the calendar

year. It is noteworthy that the books of this taxpayer were kept and its income-tax returns were made on the cash basis. (R. 60.)

There is no occasion to be concerned, as counsel for the taxpayer here appears to be (Br. pp. 26–27), for a corporation making a return on the basis of a fiscal year ending June 30, 1921. Under the provisions of Section 205 of the Revenue Act of 1921, such a corporation would in 1921 pay an income tax and profits tax for the last six months of 1920 on the basis of the provisions of the Act of 1918 and it would pay an income tax for the last six months of that period, i. e., the first six months of 1921, on the basis of the provisions of Section 243 of the Revenue Act of 1921. It would also pay the capital-stock tax imposed by the Act of 1918. It is true that its payments for 1921, the year of transition from the old taxes to the new, would be somewhat greater than would its payments in other years, but that is merely because its plan of adopting such a fiscal year in effect resulted in its paying some of the tax on the income for the year 1921 in that year instead of paying it all in the year 1922, as would a corporation which paid its tax on the basis of a calendar year.

II

THE COMMISSIONER PROPERLY INCLUDED IN THE MEASURE OF THE CAPITAL STOCK TAX FOR EACH YEAR THE THREE ITEMS APPEARING IN THE COMPANY'S STATEMENT FOR THE PRECEDING CALENDAR YEAR, REPRESENTING THE DIVIDENDS DECLARED AFTER THE END OF THAT CALENDAR YEAR AND THE "INTERIM ACCUMULATION FUND"

Under this point two questions arise: (1) Whether the items in question are included by the provision of paragraph (c) of Section 1000 of the Revenue Act of 1918, and (2) whether they are excluded by paragraph (b) of this section.

(A) The items in question are included by the provisions of paragraph (c) of Section 1000 of the Revenue Act of 1918

Paragraph (c) of Section 1000 provided that—

> The taxes imposed by this section shall apply to mutual insurance companies, and in the case of every such domestic company the tax shall be equivalent to $1 for each $1,000 of the excess over $5,000 of the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding accounting period used by such company for purposes of making its income-tax return; * * *.

It thus becomes necessary to determine in the present case whether the items in dispute may properly be classified either as "surplus or contingent reserves maintained for the general use of the business" or as "reserves the net additions to which are included in net income under the provisions of Title II."

(1) The items in question are "surplus" within the meaning of this section

Both courts below held that these items were "surplus" within the meaning of Section 1000(c)—correctly, we maintain. Whether the words in the statute "maintained for the general use of the business" modify the word "surplus" is unimportant, as surplus is, of course, maintained for the general use of the business inasmuch as it is employed in financial operations and is available to meet obligations.

We submit that the word "surplus," as used in this section, must include so much of the assets of a mutual life insurance company as remain after deducting the amount of all existing matured claims and a proper reserve for payment of insurance which will mature in the future.

In order to determine the characteristics of the items in question, it is necessary to consider the nature of mutual life insurance which is conducted on the level premium plan (as was all of the insurance issued by this company) and also the rights of the policyholders in relation to the funds of the com-

pany. The essential facts upon which these matters are based are recited in the findings (see pp. 8–11, *supra*). This Court has summarized exactly the nature and incidents of this kind of insurance in *Penn Mutual Life Insurance Co.* v. *Lederer*, 252 U. S. 523, 534, where it said:

> * * * the service performed in level-premium life insurance is both protection and investment. Premiums paid—not in the tax year, but perhaps a generation earlier—have earned so much for the co-operators, that the company is able to pay to each not only the agreed amount but also additional sums called dividends; and have earned these additional sums, in part at least, by transactions not among the members, but with others; as by lending the money of the cooperators to third persons who pay a larger rate of interest than it was assumed would be received on investments. The fact that the investment resulting in accumulation or dividend is made by a cooperative as distinguished from a capitalistic concern does not prevent the amount thereof being properly deemed a profit on the investment. * * *

In *Duffy* v. *Mutual Benefit Life Insurance Co.*, 272 U. S. 613, the Court, in holding that the legal reserves of a mutual life insurance company should be included in the computation of invested capital for purposes of the profits tax, said of legal reserves:

These assets, thus constituted, have never represented indebtedness any more than the capital of a stock corporation subscribed by its stockholders represents indebtedness. Until the maturity of a policy, the policyholder is simply a member of the corporation, with no present enforceable right against the assets. Upon the maturity of the policy he becomes a creditor with an enforceable right. Then for the first time there is an indebtedness. * * * In the meantime each member bears a relation to the mutual company analogous to that which a stockholder bears to the joint-stock company in which he holds stock. In either case, the title to the assets is in the corporation and not in the members or stockholders.

True, the amount of the reserve is carried on the books as a liability, but only as the capital stock of a stock corporation is carried on its books as a liability. In both instances, it is a form of bookkeeping to balance assets, which in the one case is contributed by the members and in the other by the stockholders. * * *

These statements are *a fortiori* true of the items in question, although they are not included in the legal reserves.

The following conclusions apply to all three of these items. They were nothing but bookkeeping items and existed as separate funds only on the

books of the company, as the company's assets were in no way segregated or in any way earmarked for investment purposes, and the company did not separately invest any sums shown in the items in question. At the end of any year no person had a right to any particular amount on account of any of the three items. Although the company's charter, the policies, and the New York insurance law all required the directors to make appropriations for dividends shortly after the end of each year if circumstances warranted so doing, the matter was left largely to the discretion of the directors, and we are aware of no case in which it has been held that the directors could be forced to declare a dividend different from what they actually did declare. None of these items constituted a trust fund, and even upon the maturity of a policy a policyholder has no right to require an accounting of the funds of the company in the absence of proof of wrongdoing or mistake. See *Equitable Life Assurance Society* v. *Brown*, 213 U. S. 25, 46–47; *Uhlman* v. *New York Life Insurance Co.*, 109 N. Y. 421; *Greeff* v. *Equitable Life Assurance Society*, 160 N. Y. 19. The rights of the policyholders to dividends and to control over the assets of the corporation are similar to the rights of stockholders in a stock corporation. See *Mayer* v. *Attorney General*, 32 N. J. Eq. 815. As the Circuit Court of Appeals observed, "While it is true that each policy provides for the declaration of those profits in

the form of dividends, it is rather as a charter—also a contract—provides for the declaration of dividends to shareholders in a stock company." (R. 187.) We find nothing in the insurance laws of New York indicating that the items in question should be considered as liabilities. The provisions of law as to when a life insurance company is to be deemed insolvent, when a mutual company may be forced to discontinue business, when a receiver shall be appointed, and as to the manner of valuing its assets and liabilities give no intimation that any of these items is to be considered as a liability. See Sections 21, 43, 82, and 86 of the New York insurance laws, pp. 89–91, *infra*. See also Section 83, which provides for the distribution of *surplus* to policyholders, and Section 87 limiting the amount of a contingency reserve which a company can maintain (pp. 90–92, *infra*).

As the three items differ from each other somewhat in their characteristic details, we will analyze them. Inasmuch as the taxes for four separate years are in controversy and the fundamental facts are the same for all years, we will discuss the items as they appear in the statement as of December 31, 1917. As Section 1000 imposes the tax on the surplus, etc., "as of the close of the preceding accounting period used by such company for purposes of making its income-tax return," and as this company made its income-tax return for the calendar year, the condition of its assets on December 31,

1917, governs the capital-stock tax for the first of the years involved—that beginning July 1, 1918.

Item 35 represented dividends declared or apportioned to annual dividend policies. These dividends were payable in 1918, and they were not declared until January 14, 1918. Consequently, Item 35 had no existence as a separate item at the end of 1917; and, at least until the directors acted some time later, the sum represented by it was merely an undesignated part of the general assets of the corporation. Until the directors acted, no policyholder had any claim to any distinct amount. The amount was appropriated from the account designated by the company as its "Undivided Surplus Account." This account was made up by adding the profits for 1917 to an amount taken from another account designated by the company as "Latent Fund for Contingencies and Dividends."

Item 36 was the amount of dividends declared or apportioned to deferred dividend policyholders payable to them during 1918. It came out of the "Interim Accumulation Fund." (The facts in regard to the "Interim Accumulation Fund" are summarized on page 10, *supra*, and the nature of this fund is also discussed on pages 44–45, below.) Although, in the normal course, all of Item 36 would be paid out during 1918 as dividends to holders of deferred dividend policies, no policyholder became entitled to a payment unless his policy was in force and he was alive at the expira-

tion of the distribution period, which would occur sometime during 1918. If his policy should lapse or he should die before that time, the amount to which he would have been entitled would go to other policyholders of the same class. Until the declaration of this dividend shown in Item 36, on January 14, 1918, no definite amount was set aside even for the group.

Item 37, the "Interim Accumulation Fund," in the statement as of December 31, 1917, consisted of amounts which had been allocated to the fund by annual appropriations of many years, including that of January 14, 1918. No policyholder or class of policyholders would have any right to any definite amount from this fund, at least until part of it was apportioned for distribution, and the first such apportionment would not be made until the early part of 1919.

We submit that the creation of the "Interim Accumulation Fund" had no legal effect. It was maintained merely to show the result of the calculations and determinations of the directors and officers of the company over a period of years. If unforeseen events should occur, the amount represented by this item could, if necessary, have been devoted to the payment of life insurance on policies which matured unexpectedly, as well as to the payment of other valid claims against the company. The same is true, we submit, of Items 35 and 36—certainly on December 31, 1917, before the divi-

dends represented by them had been declared. Not until the dividends were declared could any policyholder maintain an action to recover the dividend if the company had refused to pay it. Consequently, the amounts represented in Items 35 and 36 up to the time of the declaration of the dividend and the amounts represented in Item 37 at all times were subject to no different obligations than they would have been had they been carried in a single account entitled simply "surplus" or in the "Security Fluctuation and General Contingency Fund" which appears in the annual statement under Item 38. It is significant that the last-mentioned fund was drawn upon for the payment of part of these dividends, and it would seem that the duties of the directors as to the handling of that fund were not substantially different from their duties in regard to the surplus for any particular year. All of these funds alike were subject to distribution to policyholders proportionately to such extent as the directors felt it safe to diminish these funds.

It is not without significance, we believe, that the directors of the company expressly referred to the account from which these various dividend items were appropriated as "surplus." Thus, the resolution which appropriated $12,437,514 to the annual dividend policyholders during the year 1918 (Item 35) provided that (R. 47)—

> the remainder of the *surplus*, being the amount of $12,437,514.00, be appropriated from the *Undivided Surplus Account*, out of which shall be paid to those policies which participate annually in *surplus* on their anniversaries in 1918, a dividend * * *. (Italics ours.)

On the same day the directors set aside part of their funds to be held for the benefit of deferred dividend policyholders. By resolution it was provided that (R. 59)—

> $33,846,861.64 be credited to the Interim Accumulation Fund. The balance of the latter account will then be equal to $121,165,327.64, this being the Reserve to be held by the Company, as shown in Schedule D of the Actuaries' Report as to the disposition of the *surplus*, * * *. (Italics ours.)

Of the sum of $121,165,327.64 thus set aside from surplus for deferred dividends, the sum of $14,123,549.64 was declared as dividends payable to deferred dividend policyholders during 1918. This sum constitutes Item 36. The balance of the total sum, $107,041,778, held for the benefit of deferred dividend policyholders, whose right to dividends mature in future years, constitutes Item 37 of the company's annual report. (R. 50-51.)

The company's charter, its policies, and the agreed statement of facts, as well as the annual report of the officers to the directors, designate the

earnings during the year which are to be divided as "Surplus" or "Divisible Surplus." (R. 40–43, 61.)

Furthermore this Court has designated the funds which went into the items now under consideration as "surplus." In *New York Life Insurance Company* v. *Edwards*, 271 U. S. 109, 115, this Court said, concerning the present taxpayer—

> At the end of each year the actual insurance costs and expenses incurred are ascertained. The difference between their sum and the total of advanced payments and other income then becomes the "overpayment" or *surplus* fund for immediate *pro rata* distribution among policyholders as dividends or for such future disposition as the contracts provide. (Italics ours.)

And it has been held that dividends paid by a mutual life insurance company can be paid only from "surplus" and that funds held by such a company for the payment of dividends are "surplus." See *Fuller* v. *Metropolitan Life Ins. Co.*, 70 Conn. 647.

We submit that these designations of these items as appropriations or dispositions of "surplus" were correct.

To summarize, the three items were not liabilities except in an accounting sense, and they were analogous to surplus or undivided profits of a stock corporation.

The tax should be measured by business and financial realities and not by bookkeeping forms or mere names. *Hecht* v. *Malley*, 265 U. S. 144, 163.

Apparently there have been no decisions of any court, except those of the courts below in the instant case, construing the provisions of Section 1000 (c).[14] The Treasury Department has always construed them as requiring the inclusion of the three items in question.[15] It is also significant that the Treasury Department, in computing invested capital of mutual life insurance companies for purposes of the profits tax (under Section 207 of the Revenue Act of 1917, c. 63, 40 Stat. 300, 306, and under Section 326 of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1092) allowed the taxpayer the

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[14] Except *Metropolitan Life Ins. Co.* v. *United States*, 65 C. Cls. 149, which relates to an entirely different question under this section.

[15] No formal regulations to this effect appear to have been promulgated, but Law Opinion 1104, rendered by the Solicitor of Internal Revenue and approved by the Commissioner, published in I–2 Cumulative Bulletin (July–December, 1922), page 331, expressly decides this point. (This opinion is printed as Appendix D, pp. 80–88, *infra*.) The regulations relating to the capital-stock tax provided specifically that the tax should apply to mutual insurance companies; the language of the regulations is substantially the same as that used in the statute. See Articles 61 and 62 of Regulations 50, promulgated April 29, 1919, and Articles 23 and 24 of Regulations 50 (revised), promulgated June 21, 1920 (*infra*, pp. 78–79).

benefit of including the items in question as "paid in or earned surplus and undivided profits."[16]

The Commissioner, computing the basis for the capital stock tax, deducted from the total admitted assets as of December 31, 1917, all items appearing in that schedule in the annual statement to the Insurance Superintendent, designated as "V—Liabilities, Surplus and Other Funds," except Items 35, 36, 37, 38, 39, 47, and 48 (See R. 169–173). This form included 48 different items. Item 47 was designated "Capital paid up" and Item 48 "Unassigned funds (surplus)." In each year the company entered "0" opposite Items 47 and 48. The items which the Commissioner deducted included not

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[16] See Bulletin H, Income Tax Rulings Peculiar to Insurance Companies, published by Bureau of Internal Revenue, April 9, 1921, paragraphs 11 and 12; and *Mutual Benefit Life Insurance Co.* v. *Duffy*, 295 Fed. 881, 890 (D. N. J.). (This case was affirmed as to the point there in controversy, 3 F. (2d) 1020; 268 U. S. 686.)

The language of Section 1000 (c) was evidently patterned on that of Regulations 41, promulgated February 4, 1918, under the profits tax provisions of the Revenue Act of 1917, Art. 65 of which provided in part as follows:

"*Invested capital of insurance companies.* (a) The invested capital of a *mutual insurance company* will be deemed to consist of the sum of (1) any surplus or contingent reserves maintained for the general use of the business, plus (2) any legal [sic] reserves the net additions to which are included in the net income subject to the tax—subject to the restrictive provisions of Article 44 requiring the exclusion of tax-free assets other than obligations of the United States."

only legal reserves but also numerous reserves for various liabilities. The Commissioner also deducted the statutory exemption of $5,000 and a large amount claimed by the company as the difference between book value of assets and market value of assets. The deduction required to bring the assets down to such market value, which was considerably less than the market value as figured in the statements to the Insurance Superintendent, in each year more than equalled the total amount shown in Items 38 and 39, and the tax was consequently based upon a valuation which was somewhat less than the aggregate amount of Items 35, 36, and 37.

(2) If the items in question do not come within the description of "surplus as to contingent reserves maintained for the general use of the business," Item 37 at least comes within the description "any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding accounting period used by such company for purposes of making its income-tax return"

It is true that the word "reserves" in its technical sense would not include any of the items in question. See *Maryland Casualty Co.* v. *United States*, 251 U. S. 342, 350–352. But it can not have this meaning in the last category mentioned in Section 1000(c) because there are no reserves in the strict sense "the net additions to which are included in net income under the provisions of Title II." It is noteworthy that in the resolutions of the directors (R. 62, 66, 70, 73–74), the "Interim Accumulation Fund" is characterized as a "Reserve."

We submit that it was in fact a "reserve" as that word was used in the statute, and that it was properly used by the Commissioner as a basis for assessing the capital stock tax, since it was a reserve the net addition to which was included in net income.

The only deductions from net income for purposes of income tax peculiar to life insurance companies were those provided in Section 233 (a) (1) and Section 234 (a) (10) of the Revenue Act of 1918. Section 233 (a) (1) provided:

> In the case of life insurance companies there shall not be included in gross income such portion of any actual premium received from any individual policyholder as is paid back or credited to or treated as an abatement of premium of such policyholder within the taxable year.

Section 234 (a) (10) provided for the deduction of—

> The net addition required by law to be made in the taxable year to reserve funds * * * and the sums other than dividends paid within the taxable year on policy and annuity contracts; * * *.

Under Section 233 (a) (1) the amount shown in the annual statement of one year as Item 35 was deductible from gross income of the following year, and this sum was in fact deducted from gross income. (R. 60.) Likewise, under the same section, and under the decision in *Penn Mutual Insurance Co.* v. *Lederer*, 252 U. S. 523, so much of Item 36 (appearing in the report of December 31, 1917)

as was equivalent to the amount received in 1918 as premiums from those deferred dividend policyholders who received dividends during 1918 could be excluded from gross income for the year 1918, and under this provision 4% of Item 36 was in fact so excluded from the taxable gross income. (R. 60.)

But no part of Item 37, the "Interim Accumulation Fund," was excluded from gross income. (R. 60.) And since that fund was not a legal reserve fund to which additions were required to be made by law, the net additions to it were not excludable from gross income under Section 234 (a) (10).

In *New York Life Insurance Co.* v. *Edwards, Collector,* 271 U. S. 109, the Court held that the redundancy of the deferred dividend policyholders' payments of premiums which were not returned to them during the taxable year in question could not be deducted in computing the income tax. The Court said (p. 116):

> * * * Here it is insisted that within the meaning of the quoted provision each deferred dividend policyholder's overpayment was actually credited to him during the year; but we can not accept this theory. The aggregate of all such payments was held for distribution among policyholders alive at the end of the period. The receipts for the year were not really diminished.

Consequently, the sums appearing in the annual statement each year as Item 37 were "reserves, the net additions to which are included in net income"

as that term is used under Section 1000 (c) of the Revenue Act of 1918. We submit that if the "Interim Accumulation Fund" did not constitute "surplus," it must be regarded as "reserves."

Counsel for the taxpayer in his brief has asserted that the tax upon it is enormous and has given figures showing the value of the capital stock of certain other stock companies which were mutualized.[17] Counsel and the Circuit Court of Appeals assert that the Act, as applied by the Commissioner, results in inequality between mutual and stock companies. If Congress has imposed on mutual companies a tax which operates in this way, the question of fairness of the tax and discrimination between stock companies and mutual companies is immaterial. But in view of these assertions, it may not be out of place for us to point out that such generalizations as we are able to make about the matter seem to negative these conclusions. During the years in question apparently there were no very large stock life insurance companies—none in any way comparable in size to the New York Life Insurance Company. The Bureau of Internal Revenue has, at our request, prepared a table designed to show the operation of the tax as to mutual companies and stock

[17] No information in regard to these matters appears in the record, and we have not attempted to ascertain the significance of this matter or the explanations for it. The whole argument seems to us inadmissible.

companies of approximately the same size. In order to make this comparison, it has compared with twelve stock companies twelve mutual companies of approximately the same size as determined by gross assets during one of the years here involved, i. e., 1921. We realize, of course, that the comparison which it affords is necessarily rough, and there may be ground for many explanations and distinctions. But the significant ultimate fact to be deduced from the comparison is that, although the total gross assets of the twelve mutual companies which appear in the table substantially exceeded the total gross assets of the stock companies appearing thereon, the total capital stock taxes of the mutual companies (computed in accordance with our contention herein) were less than those paid by the stock companies. And the tax paid by the New York Life Insurance Company is comparable to that paid by the stock companies in proportion to the amount of the gross assets of the companies.

(B) The items in question are not excluded by Section 1000 (b)

The taxpayer here contends that the provisions of paragraph (b) of Section 1000 of the Revenue Act of 1918 apply to mutual insurance companies, and, therefore, since the company is required by contract to maintain or hold its surplus for apportionment among its policyholders, such surplus must be excluded from the basis for determining the tax. This paragraph provides:

> In computing the tax in the case of insurance companies such deposits and reserve funds as they are required by law or contract to maintain or hold for the protection of or payment to or apportionment among policyholders shall not be included.

We contend that this paragraph is not applicable to mutual companies, and both courts below so held.

The meaning of the language used in Section 1000 of the Revenue Act of 1918 may be clarified by an examination of the history of the capital stock-tax provision. Section 407 of the Revenue Act of 1916 (*infra*, pp. 59–60) placed a special excise tax upon corporations, including insurance companies, and fixed the value of the capital stock as the measure of the tax. Since mutual insurance companies have no capital stock, the Treasury Department at first ruled that they were not taxable under that section. See Article 2 (b) of Regulations 38, promulgated October 19, 1916, under the Revenue Act of 1916.[18]

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[18] This article reads as follows:

"Inasmuch as the basis of tax is the fair value of the stock of a corporation, mutual insurance companies and other associations not having capital stock represented by shares will also be exempt from tax, in the absence of a basis for the computation of the tax."

By Article 3 of Regulations 38 (Revised), promulgated August 9, 1918 (*infra*, p. 77), this ruling was reversed and it was provided that mutual insurance companies were subject to the tax. The District Court for the District of Massachusetts has recently sustained this regulation and held that a mutual fire insurance company was subject to the capital stock tax under the 1916 Act. *Lumber Mutual Fire Ins. Co.* v. *Malley* (D. Mass., decided December 1, 1930, not yet reported).

When H. R. 12863, 65th Congress, 3d Session, which later became the Revenue Act of 1918, passed the House, Section 1000 was substantially the same as Section 407 of the Revenue Act of 1916. When the bill reached the Senate there were substituted (Amendment No. 186) in lieu of Section 1000, Sections 245, 246, and 247, placing a tax upon the income of insurance companies. As affecting other corporations, the Finance Committee of the Senate recommended that Section 1000 be so amended as to make the basis of the tax the amount of the net assets of the corporation as shown by its books. Senate Report No. 617, at pp. 17–18 (*infra*, p. 69). In conference, Sections 245, 246, and 247, as added by the Senate, were eliminated. See comment on Amendment No. 186 in House Report 1037, 65th Congress, 3d Session, p. 60 (*infra*, p. 70). Section 1000 was restored to its original form except that paragraph (c) was amended by adding the provision making the tax specifically applicable to mutual insurance companies. See comment on Amendments Nos. 488–492 in House Report 1037, p. 84 (*infra*, pp. 70–72).

There can be no doubt that Congress intended to impose a tax upon mutual insurance companies, and that the specific language of paragraph (c) was added to remove the doubt on this question which had existed under the 1916 Act. The provisions of paragraph (b) were taken with substan-

tially no change from Section 407 of the Revenue Act of 1916 (*infra*, p. 59) and were included in Section 1000 of H. R. 12863, *supra*, as it passed the House. As shown by the legislative history, paragraph (c) was added to Section 1000 by the conference committee as a special provision applying to mutual insurance companies. It would seem clear, therefore, that paragraph (b) was intended to apply only to insurance companies having capital stock, while paragraph (c) prescribes the basis for determining the tax to be imposed upon mutual insurance companies having no capital stock. Otherwise mutual insurance companies would again be likely to escape taxation, and the provisions of paragraph (c) would be nullified.

The arrangement of the provisions of Section 1000 (printed in full on pp. 61–62 *infra*) also indicates that provisions of paragraph (b) do not qualify the provisions of paragraph (c). The parts of paragraph (c) in question are isolated from (b) by another provision so wholly distinct that its placement there would be unreasonable if what followed it were intended to refer back to what preceded it. But in any event the more specific provisions of (c) would supersede those of (b) rather than be limited by those of (b). Fair interpretation often requires that one of two provisions be read broadly enough to override the other rather than be limited to a meaning not inconsistent with the other.

CONCLUSION

We maintain that the judgment of the Circuit Court of Appeals as affecting the tax for the first three periods involved should be affirmed, but that as relating to the tax for the fourth period it should be reversed.

Respectfully submitted.

THOMAS D. THACHER,
Solicitor General.

G. A. YOUNGQUIST,
Assistant Attorney General.

CLAUDE R. BRANCH,
SEWALL KEY,
JOHN H. MCEVERS,
Special Assistants to the Attorney General.

ERWIN N. GRISWOLD,
Attorney.

C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue,

EDWARD H. HORTON,
Special Attorney,
Bureau of Internal Revenue,

SAMUEL C. COLEMAN,
Assistant United States Attorney,
Of Counsel.

FEBRUARY, 1931.

APPENDIX A

STATUTES INVOLVED

The Revenue Act of 1916, c. 463, 39 Stat. 756, 789–790, 792, provided in part as follows:

SPECIAL TAXES

SEC. 407. That on and after January first, nineteen hundred and seventeen, special taxes shall be, and hereby are, imposed annually, as follows, that is to say:

Every corporation, joint-stock company or association, now or hereafter organized in the United States for profit and having a capital stock represented by shares, and every insurance company, now or hereafter organized under the laws of the United States, or any State or Territory of the United States, shall pay annually a special excise tax with respect to the carrying on or doing business by such corporation, joint-stock company or association, or insurance company, equivalent to 50 cents for each $1,000 of the fair value of its capital stock and in estimating the value of capital stock the surplus and undivided profits shall be included: *Provided,* That in the case of insurance companies such deposits and reserve funds as they are required by law or contract to maintain or hold for the protection of or payment to or apportionment among policyholders shall not be included. The amount of such annual tax shall in all cases be computed on the basis of the fair

average value of the capital stock for the preceding year: *Provided,* That for the purpose of this tax an exemption of $99,000 shall be allowed from the capital stock as defined in this paragraph of each corporation, joint-stock company or association, or insurance company: *Provided further,* That a corporation, joint-stock company or association, or insurance company, actually paying the tax imposed by section three hundred and one of Title III of this Act shall be entitled to a credit as against the tax imposed by this paragraph equal to the amount of the tax so actually paid: *And provided further,* That this tax shall not be imposed upon any corporation, joint-stock company or association, or insurance company not engaged in business during the preceding taxable year, or which is exempt under the provisions of section eleven, Title I, of this Act.

* * * * *

SEC. 409. That all administrative or special provisions of law, including the law relating to the assessment of taxes, so far as applicable, are hereby extended to and made a part of this title, and every person, firm, company, corporation, or association liable to any tax imposed by this title, shall keep such records and render, under oath, such statements and returns, and shall comply with such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may from time to time prescribe.

The Revenue Act of 1918, c. 18, 40 Stat. 1057, 1126, provided in part as follows:

TITLE X.—SPECIAL TAXES

SEC. 1000. (a) That on and after July 1, 1918, in lieu of the tax imposed by the first subdivision of section 407 of the Revenue Act of 1916—

(1) Every domestic corporation shall pay annually a special excise tax with respect to carrying on or doing business, equivalent to $1 for each $1,000 of so much of the fair average value of its capital stock for the preceding year ending June 30 as is in excess of $5,000. In estimating the value of capital stock the surplus and undivided profits shall be included;

(2) Every foreign corporation shall pay annually a special excise tax with respect to carrying on or doing business in the United States, equivalent to $1 for each $1,000 of the average amount of capital employed in the transaction of its business in the United States during the preceding year ending June thirtieth.

(b) In computing the tax in the case of insurance companies such deposits and reserve funds as they are required by law or contract to maintain or hold for the protection of or payment to or apportionment among policyholders shall not be included.

(c) The taxes imposed by this section shall not apply in any year to any corporation which was not engaged in business (or in the case of a foreign corporation not engaged in business in the United States) during the preceding year ending June 30, nor to any corporation enumerated in section 231. The taxes imposed by this section shall

apply to mutual insurance companies, and in the case of every such domestic company the tax shall be equivalent to $1 for each $1,000 of the excess over $5,000 of the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding accounting period used by such company for purposes of making its income tax return. *Provided,* That in the case of a foreign mutual insurance company the tax shall be equivalent to $1 for each $1,000 of the same proportion of the sum of such surplus and reserves, which the reserve fund upon business transacted within the United States is of the total reserve upon all business transacted, as of the close of the preceding accounting period used by such company for purposes of making its income tax return.

(d) Section 257 shall apply to all returns filed with the Commissioner for purposes of the tax imposed by this section.

* * * * *

SEC. 1305. That all administrative, special, or stamp provisions of law, including the law relating to the assessment of taxes, so far as applicable, are hereby extended to and made a part of this Act, and every person liable to any tax imposed by this Act, or for the collection thereof, shall keep such records and render, under oath, such statements and returns, and shall comply with such regulations as the Commissioner, with the approval of the Secretary, may from time to time prescribe.

* * * * *

The Revenue Act of 1921, c. 136, 42 Stat. 227, 261, 294, 295, 320, 321, provided in part as follows:

TAXES ON INSURANCE COMPANIES

* * * * *

SEC. 243. That in lieu of the taxes imposed by sections 230 and 1000 and by Title III, there shall be levied, collected, and paid for the calendar year 1921 and for each taxable year thereafter upon the net income of every life insurance company a tax as follows:

(1) In the case of a domestic life insurance company, the same percentage of its net income as is imposed upon other corporations by section 230;

(2) In the case of a foreign life insurance company, the same percentage of its net income from sources within the United States as is imposed upon the net income of other corporations by section 230.

* * * * *

TITLE X.—SPECIAL TAXES

CAPITAL STOCK TAX

SEC. 1000. (a) That on and after July 1, 1922, in lieu of the tax imposed by section 1000 of the Revenue Act of 1918—

(1) Every domestic corporation shall pay annually a special excise tax with respect to carrying on or doing business, equivalent to $1 for each $1,000 of so much of the fair average value of its capital stock for the preceding year ending June 30 as is in excess of $5,000. In estimating the value of capital stock the surplus and undivided profits shall be included;

(2) Every foreign corporation shall pay annually a special excise tax with respect to carrying on or doing business in the United States, equivalent to $1 for each $1,000 of the average amount of capital employed in the transaction of its business in the United States during the preceding year ending June 30.

(b) The taxes imposed by this section shall not apply in any year to any corporation which was not engaged in business (or, in the case of a foreign corporation, not engaged in business in the United States) during the preceding year ending June 30, nor to any corporation enumerated in section 231, nor to any insurance company subject to the tax imposed by section 243 or 246.

(c) Section 257 shall apply to all returns filed with the Commissioner for purposes of the tax imposed by this section.

* * * * *

TITLE XIV.—GENERAL PROVISIONS

REPEALS

SEC. 1400. (a) That the following parts of the Revenue Act of 1918 are repealed, to take effect (except as otherwise provided in this Act) on January 1, 1922, subject to the limitations provided in subdivision (b):

Title II (called "Income Tax") as of January 1, 1921;

Title III (called "War-Profits and Excess-Profits Tax") as of January 1, 1921;

Title IV (called "Estate Tax") on the passage of this Act;

Title V (called "Tax on Transportation and Other Facilities, and on Insurance");

Sections 628, 629, and 630 of Title VI (being the taxes on soft drinks, ice cream, and similar articles);

Title VII (called "Tax on Cigars, Tobacco, and Manufactures Thereof");

Title VIII (called "Tax on Admissions and Dues");

Title IX (called "Excise Taxes");

Title X (called "Special Taxes");

Title XI (called "Stamp Taxes");

Title XII (called "Tax on Employment of Child Labor") as of January 1, 1921; and

Sections 1314, 1315, 1316, 1317, 1319, and 1320 of Title XIII (being certain administrative provisions) on the passage of this Act.

(b) The parts of the Revenue Act of 1918 which are repealed by this Act shall (unless otherwise specifically provided in this Act) remain in force for the assessment and collection of all taxes which have accrued under the Revenue Act of 1918 at the time such parts cease to be in effect, and for the imposition and collection of all penalties or forfeitures which have accrued or may accrue in relation to any such taxes. In the case of any tax imposed by any part of the Revenue Act of 1918 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act. The unexpended balance of any appropriation heretofore made and now available for the administration of any such part of the Revenue Act of 1918 shall be available for the administration of this Act or the corresponding provision thereof.

Section 13 of the Revised Statutes (U. S. C., Title 1, Sec. 29) provides:

> The repeal of any statute shall not have the effect to release or extinguish any penalty, forfeiture, or liability incurred under such statute, unless the repealing act shall so expressly provide, and such statute shall be treated as still remaining in force for the purpose of sustaining any proper action or prosecution for the enforcement of such penalty, forfeiture, or liability.

The Act of October 1, 1890, c. 1244, Sec. 53, 26 Stat. 567, 624 (U. S. C., Title 26, Sec. 186), provides in part as follows:

> That all special taxes shall become due on the first day of July, eighteen hundred and ninety-one, and on the first day of July in each year thereafter, or on commencing any trade or business on which such tax is imposed. In the former case the tax shall be reckoned for one year; and in the latter case it shall be reckoned proportionately, from the first day of the month in which the liability to a special tax commenced to the first day of July following. * * * And it shall be the duty of special taxpayers to render their returns to the deputy collector at such times within the calendar month in which the special tax liability commenced as shall enable him to receive such returns, duly signed and verified, not later than the last day of the month, except in cases of sickness or absence, as provided for in section three thousand one hundred and seventy-six of the Revised Statutes.

APPENDIX B

REPORTS OF CONGRESSIONAL COMMITTEES

REVENUE ACT OF 1916

The report of the Committee on Finance to the Senate (Senate Report No. 793, 64th Congress, 1st Session, p. 7) contains the following:

> Your committee recommends a license tax of 50 cents upon each thousand dollars of capital, surplus, and undivided profits of corporations, with an exemption of $99,000 of the capital, surplus, and undivided profits of each corporation. The committee amendment also exempts from this tax corporations actually paying the tax imposed by section 41, Title III, of this act (munitions tax) to an amount not in excess of the munitions tax so actually paid. It also provides that this tax shall not be imposed upon any corporation not engaged in business or which had no net income as defined in Title I of this act during the preceding taxable year, or which was exempt under the provision of section 11, Title I, of this act (income tax).

The Conference Report (House Report No. 1200, 64th Congress, 1st Session, p. 37) contains the following:

> Amendment No. 206: The Senate provides that corporations, joint-stock companies, and associations shall pay 50 cents for each $1,000 of capital stock, surplus, and undivided profits used in any of the activities

or functions of their business, including such sums of capital stock, surplus, and undivided profits as may be invested in or loaned upon stocks, bonds, mortgages, real estate, or other securities. The House recedes from its disagreement to this amendment with an amendment providing as follows: "Every corporation, joint-stock company, or association now or hereafter organized in the United States for profit and having a capital stock, and every insurance company now or hereafter organized under the laws of the United States, or any State or Territory of the United States, shall pay annually a special excise tax with respect to the carrying on or doing business of such corporation, joint-stock company, or association, or insurance company, equivalent to 50 cents for each $1,000 of the fair value of its capital stock, and in estimating the amount of capital stock, surplus and undivided profits shall be included." The amendment further provides that in the case of an insurance company, such deposits and reserve funds as they are required by law or contract to maintain or hold for the protection of or payment to or apportionment among policyholders shall not be included in assessing the tax upon the fair value of the capital stock. The amendment allows an exemption of $99,000 from the capital stock. The amendment further provides that a nonresident corporation doing business in the United States shall pay a tax equivalent to 50 cents for each $1,000 of the capital actually invested in the transaction of this business in the United States, and contains the exemption for nonresident insurance companies the same as that given resident insurance companies. It also allows a deduction for nonresident companies,

from the amount of capital so invested, equal to such proportion of $99,000 as the amount so invested bears to the total amount invested in the transaction of business in the United States or elsewhere.

Revenue Act of 1918

The report of the Committee on Finance of the Senate (Senate Report No. 617, 65th Congress, 3d Session, pp. 9, 17–18) contains the following:

LIFE INSURANCE COMPANIES

A new basis is recommended for the taxation of life insurance companies (Pt. IV, secs. 245, 246, 247). The tax is in form an income tax, but is imposed upon a net income defined with special reference to the peculiar conditions of the business of life insurance. Roughly, it consists of the gross income from interest, dividends, and rents less tax-free interest, investment expenses, and taxes and other expenses paid exclusively in connection with real estate owned by the company. In the case of a domestic life insurance company there is also a specific deduction of $2,000. Thus the tax falls upon the true income of the company; that is, its income from investments; and the rate is so fixed that this tax takes the place of the income tax, war excess-profits tax, capital-stock tax, and the tax on the issuance of policies. It will yield considerably more revenue than the taxes which it is designed to replace, and has the great merit of simplicity and certainty. Above all, it avoids the almost insuperable difficulty of defining the invested capital of a life insurance company for purposes of the war excess-profits tax.

* * * * *

The House bill provided for the continuance of the capital-stock tax on the basis of the fair average value of the capital stock of the corporation for the preceding year. The determination of fair average value has proved in administration to be very difficult. The committee has accordingly provided that the basis of the tax shall be the amount of the net assets of the corporation as shown by its books. It is believed that this basis of levying the tax is just and that the change will not lead to any reduction of the revenue from this source.

The report of the Conference Committee (House Report No. 1037, 65th Congress, 3d Session, pp. 36, 60, 84) contains the following:

Amendment No. 186: This amendment added a new "Part" to the income-tax title and provided a separate tax on the investment income of life insurance companies and mutual insurance companies in lieu of all other taxes imposed in the bill upon such companies; and the Senate recedes.

* * * * *

Amendment No. 488: The House bill imposed upon a domestic corporation an annual excise tax equivalent to $1 for each $1,000 of so much of the fair average value of its capital stock for the preceding year as is in excess of $5,000. It also provided that in estimating the value of the capital stock the surplus and undivided profits should be included. This is the basis of the tax under the present law, with the rate increased 100 per cent. The Senate amendment changes the basis of the tax from the fair average value of the capital stock to the

amount of the net assets shown on the books as of the close of the preceding income-tax year; and the Senate recedes.

Amendment No. 489: The House bill based the capital stock tax in the case of foreign corporations upon the average amount of "capital actually invested" in the United States. The Senate amendment changes this basis and places this tax upon the average amount of "capital employed" in the United States; and the House recedes.

Amendment No. 490: This amendment, as part of the Senate's general plan of insurance taxation, strikes out the House provisions relating to the computation of the capital stock tax in the case of insurance companies; and the Senate recedes.

Amendment No. 491: This amendment is a clerical change; and the Senate recedes.

Amendment numbered 492:

That the House recede from its disagreement to the amendment of the Senate numbered 492, and agree to the same with an amendment as follows:

In lieu of the matter inserted by said amendment insert a period and the following: *The taxes imposed by this section shall apply to mutual insurance companies, and in the case of every such domestic company the tax shall be equivalent to $1 for each $1,000 of the excess over $5,000 of the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in net income under the provisions of Title II, as of the close of the preceding accounting period used by such company for purposes of making its income tax return: Provided, That in the case of a foreign mutual insurance company the tax shall be equivalent to $1 for each $1,000 of the same*

proportion of the sum of such surplus and reserves, which the reserve fund upon business transacted within the United States is of the total reserve upon all business transacted, as of the close of the preceding accounting period used by such company for purposes of making its income tax return; and the Senate agree to the same.

Amendment No. 492: This amendment, as part of the Senate's general plan of insurance taxation, specifically exempts insurance companies from the capital stock tax. The House recedes with an amendment making the tax specifically applicable to mutual insurance companies and providing that in the case of every such domestic company the tax shall be based upon the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in the net income under the provisions of Title II, as of the close of its preceding income tax year; and providing that in the case of a foreign mutual insurance company the tax shall be based upon the same proportion of the sum of such surplus and reserve, which the reserve fund upon business transacted within the United States is of the total reserve upon all business transacted.

Revenue Act of 1921

The report of the Committee on Ways and Means to the House (House Report No. 350, 67th Congress, 1st Session, p. 14) contains the following:

LIFE INSURANCE COMPANIES

Sections 242–246: The provisions of the present law applicable to life insurance companies are imperfect and productive of con-

stant litigation. Moreover, the taxes paid by life insurance companies under the income tax are inadequate. It is accordingly proposed in lieu of all other taxes to tax life insurance companies on the basis of their investment income from interest, dividends, and rents, with suitable deduction for expenses fairly chargeable against such investment income. The new tax would yield a larger revenue than the taxes which it is proposed to replace.

The report of the Committee on Finance to the Senate (Senate Report No. 275, 61st Congress, 1st Session, pp. 20, 30) contains the following:

TAXES ON LIFE INSURANCE COMPANIES

Sections 242–246 provide a new plan for the taxation of life insurance companies, substantially similar to the plan embodied in the revenue act of 1918 as first adopted by the Senate. The provisions of the present law applicable to life insurance companies are imperfect and productive of constant litigation. The proposed plan would tax life insurance companies on the basis of their investment income from interest, dividends, and rents, with suitable deductions for expenses fairly chargeable against such investment income. The new tax would take the place of the present income and excess-profits taxes for the year 1921, and life insurance companies would share with other insurance companies in the repeal in the year 1922 of the capital stock tax and the taxes imposed by section 503. The new tax will yield a larger revenue than the taxes which it is proposed to replace.

* * * * *

REPEAL OF CAPITAL-STOCK TAX

Section 1000 provides for the repeal of the capital-stock tax imposed by section 1000 of the revenue act of 1918 after June 30, 1922.

APPENDIX C

REGULATIONS OF THE TREASURY DEPARTMENT

Regulations 38, promulgated October 19, 1916, under the capital stock tax provisions of the Revenue Act of 1916, provided in part as follows:

CORPORATIONS EXEMPT

CORPORATIONS AND ASSOCIATIONS EXEMPT

ART. 2. (*a*) The following corporations, joint-stock companies or associations, or insurance companies, which are exempt from income tax under the provisions of section 11, Title I, are also specifically exempt from the capital-stock tax under section 407, Title IV, of this act:

* * * * *

MUTUAL COMPANIES EXEMPT

(*b*) Inasmuch as the basis of tax is the fair value of the stock of a corporation, mutual insurance companies and other associations not having capital stock represented by shares will also be exempt from tax, in the absence of a basis for the computation of the tax.

RETURNS

* * * * *

ART. 3. (a) Section 3237, Revised Statutes, as amended by section 53 of the act of October 1, 1890 (26 Stats., 567) provides

"that all special taxes shall become due on the 1st day of July, 1891, and on the 1st day of July in each year thereafter, or on commencing any trade or business on which such tax is imposed. In the former case the tax shall be reckoned for one year, and in the latter case it shall be reckoned proportionately from the 1st day of the month in which the liability to a special tax commenced to the 1st day of July following." The capital-stock tax, therefore, which becomes effective January 1, 1917, will be payable in January, 1917, on returns to be made during that month for the six months ending June 30, 1917. In July, 1917, and annually in July thereafter, returns must again be made and the tax paid for the ensuing fiscal year.

* * * * * *

Regulations 38 (Revised), promulgated August 9, 1918, under the capital-stock tax provisions of the Revenue Act of 1916, provided in part:

ARTICLE 1. *Due date.*—The tax became effective January 1, 1917, and is to be paid annually in advance for each year beginning July 1, except as to the first payment for the six months ending June 30, 1917. Special taxes, of which this is one, become due on the 1st day of July in each year, or on commencing any trade or business on which such tax is imposed. In the former case the tax is reckoned for one year, and in the latter case it is reckoned proportionately from the first day of the month in which the liability to a special tax commenced to the 1st day of July following. But see Article 11. No tax is refundable if a corporation ceases to do business during the year.

* * * * * *

ART. 3. *Scope of tax: Insurance companies.*—The tax also applies to insurance companies which are organized under a statute or derive from that source some quality or benefit not existing at the common law, irrespective of whether or not they are organized for profit or have a capital stock represented by shares. Mutual and participating plan companies are included. A mutual protective association organized under a statute, whose only source of revenue is the assessments paid by its members and whose net income for each year is paid into a reserve fund, constituting the sole resource of the company, aside from current assessments, for the payment of losses, is an insurance company within the meaning of the statute.

Regulations 50, promulgated April 29, 1919, under the capital-stock tax provisions of the Revenue Act of 1918, provided in part:

ARTICLE 1. *Due date of tax.*—The tax became effective as of July 1, 1918, and is to be paid annually in advance for each year beginning July 1, in lieu of the capital-stock tax imposed by the Revenue Act of 1916. The tax for the first year ending June 30, 1919, although necessarily not payable in advance, must be paid upon notice and demand by the collector. See article 111. Special taxes, of which this is one, become due on the 1st day of July in each year, or on commencing any trade or business on which such tax is imposed. In the former case the tax is reckoned for one year, and in the latter case it is reckoned proportionately from the first day of the month in which the liability to a special tax commenced to the 1st day of July following. But see article 51. No tax is re-

fundable if a corporation ceases to do business during the year.

* * * * *

ART. 61. *Mutual insurance company.*—The tax applies to domestic and foreign mutual insurance companies. A mutual protective association organized under a statute, whose only source of revenue is the assessments paid by its members and whose net income for each year is paid into a reserve fund, constituting the sole resource of the company, aside from current assessments, for the payment of losses, is an insurance company within the meaning of the statute. A voluntary unincorporated association of employees formed for the purpose of relieving sick and aged members and the dependents of deceased members is an insurance company, whether the fund for such purpose is created wholly by membership dues or partly by contributions from the employer.

ART. 62. *Domestic mutual insurance company—rate of tax.*—The tax is $1 for each full $1,000 of the excess over $5,000 of the sum of (a) the surplus or contingent reserves maintained for the general use of the business and (b) any reserves the net additions to which are included in net income for the purpose of the income tax, in both cases figured as of the close of the last taxable year of the company. The net addition required by law to be made within the taxable year to reserve funds, including in the case of assessment insurance companies the actual deposit of sums with State or Territorial officers pursuant to law as additions to guarantee or reserve funds and, in the case of corporations issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium

payment plan continuing for life and not subject to cancellation, including such portion of the net addition not required by law made within the taxable year to reserve funds as is needed for the protection of the holders of such combination policies, is not included in net income for the purpose of the income tax. See Regulations 45 and particularly articles 568–570 thereof.

In Regulations 50 (Revised), promulgated June 21, 1920, under the capital stock tax provisions in the Revenue Act of 1918, Articles 1, 23, and 24 are substantially the same as Articles 1, 61, and 62, respectively, of Regulations 50 set out above.

Regulations 64 (1922 ed.) promulgated June 15, 1922, under the capital stock tax provisions of the Revenue Act of 1921, provided in part:

ARTICLE 1. *The law.*—The main provisions of existing law with respect to this tax are embodied in section 1000 of the Revenue Act of 1921, referred to hereinafter as the act.

ART. 2. *Due date of tax.*—The act was approved November 23, 1921, but the tax is effective from July 1, 1922, except upon the incorporation of an individual or partnership business (see art. 32). This is a special tax and like all special taxes is due and payable annually in advance from July 1 of each year. No portion of the tax so paid is refundable to a corporation which ceases to do business during the year.

APPENDIX D

LAW OPINION 1104

Law Opinion 1104, rendered by the Solicitor of Internal Revenue and approved by the Commission, published in I-2 Cumulative Bulletin (July-December, 1922), p. 331, is as follows:

LIABILITY OF MUTUAL LIFE INSURANCE COMPANIES TO CAPITAL-STOCK TAX

Informal request has been made for a reconsideration of Solicitor's Opinion 101 and Law Opinion 1078, relative to the liability of mutual life insurance companies to capital-stock tax under the provisions of section 1000 of the Revenue Act of 1918. It is requested that a single opinion be written which will supersede Solicitor's Opinion 101 and Law Opinion 1078, and which will within itself declare the proper method of assessing and collecting such capital-stock tax.

* * * * *

Four distinct questions are involved:

I

Certain mutual life insurance companies claim that in computing the capital-stock tax, paragraph (b) of section 1000 is applicable, irrespective of whether paragraph (c) is to be applied. Opinion is requested as to the correctness of this contention.

It has been suggested that paragraph (b) applies only to nonmutual companies and paragraph (c) to mutual companies.

II

It is contended by the companies that they should be assessed on the market value of their assets, and that the depreciation, below the amortized value, of assets carried in their reserves, whether required or not required, should be deducted in estimating the amount of the taxable surplus.

III

The companies contend that certain funds set up to meet certain dividend charges are exempt from tax because they are funds held for payment to certain policyholders and are not surplus or contingent reserves maintained for the general use of the business nor reserves the net additions to which are included in net income for income tax purposes.

IV

It further appears that the N Company is peculiar in that there is still outstanding 100x dollars of its capital stock. Dividends on this stock are limited by charter to 7 per cent. Although nominally a stock company, it is operated entirely on a mutual basis and is to all intents and purposes a mutual company. Opinion is requested as to whether or not this company should be classed as a mutual company or as a nonmutual company.

Paragraph (c) of section 1000 subjects to tax those reserves "the net additions to which are in-

cluded in net income under the provisions of Title II." The provisions of Title II referred to are found in paragraph (a) (10) of section 234 (supra). Under section 234(a) (10) "The net addition required by law to be made within the taxable year to reserve funds" is deductible in computing net income. Apparently "included in net income" is intended to mean "not deductible from gross income in computing net income."

The four questions stated above should be decided as follows:

I

The tax imposed by section 1000 of the Revenue Act of 1918 is a capital-stock tax and its provisions are designed generally to tax corporations having a capital stock divided into shares. Mutual insurance companies have, properly speaking, no capital stock represented by shares and are cooperative as distinguished from stock companies organized for profit. For this reason Congress has provided for the taxation of mutual insurance companies a rule different from that laid down in paragraphs (a) and (b). This rule is found in sentences quoted from paragraph (a). It is, therefore, held that nonmutual insurance companies should be assessed under the provisions of paragraphs (a) and (b) of section 1000 of the Revenue Act of 1918, and that mutual insurance companies should be assessed under the provisions of paragraph (c) of said section. This construction of the statute is the one adopted in articles 22 and 23 of Regulations 50 (revised).

The ruling herein made works an apparent hardship upon certain mutual insurance companies and

especially upon those which have large deferred dividend reserves. Such companies must include such reserves in their surplus if they are held subject to tax under the provisions of paragraph (c). Stock companies, on the other hand, which are liable to tax under the provisions of paragraph (b), are not liable to tax upon such portion of their surplus as is included in such deferred dividend reserve. This inequality of the tax burden is inherent in the taxing statute and can not be removed by interpretation.

In L. O. 1032 it was held in construing section 38 of the Act of August 5, 1909, and paragraph G (a) and (b) of the Act of October 3, 1913, that the words "reserve fund 'required by law' included not only reserves required by express statutory provisions, but also reserves required by the rules and regulations of State insurance departments, when promulgated in the exercise of an appropriate power conferred by statute; but do not include assets required to be held for the ordinary running expenses of the business, such as taxes, salaries, reinsurance, and unpaid brokerage." Under the language of the Act of 1909, companies may "deduct the net addition, if any, required by law to be made within the year to reserve funds." The language of the Act of 1913 is "by deducting * * * the net addition, if any, required by law to be made within the year to reserve funds." The language of the Act of 1916 is "by deducting * * * the net addition, if any, required by law to be made within the year to reserve funds." The language of these three Acts is almost identical with the language of section 234 (a) (10) of the

Act of 1918, and it is, therefore, held that the ruling of L. O. 1032 is applicable to the construction of Section 234 (a) (10) of the Revenue Act of 1918.

II

The contention of the mutual insurance companies that in making capital-stock tax returns they should be allowed to value securities held by them as investments at the market price instead of at the amortized value is believed to be sound. The capital-stock tax is imposed upon so much of the "fair average value" of the capital stock of a corporation for the preceding year ending June 30 as is in excess of $5,000. In estimating the fair average value of the assets of corporations other than insurance companies securities are valued at their fair market value. There does not appear to be any reason why the same rule should not be applied to insurance companies.

However, under the rule heretofore laid down in Solicitor's Opinion 101 and Law Opinion 1078, only the assets in excess of the amount of the legal reserves are permitted to be valued at their market value for capital-stock tax purposes. The mutual life insurance companies contend that there is no reason for the rule; that the reserves required to be kept under the various State insurance laws are based upon certain percentages of the amount of premiums paid in by policyholders; and that the amount of such reserves bear no relation whatever to the amount of the assets. It is, therefore, contended that the "fair average value" of the assets of mutual insurance companies should be the fair market value of their assets. It is contended that

if the securities were enhanced in value the Bureau would tax the whole increase and not merely that portion of the increase in excess of the legal reserves. This office has carefully reconsidered this contention and is of the opinion that it is well taken. It is held that the total admitted assets of mutual insurance companies should be valued at their fair market value before any deductions are made. Accordingly, in determining the amount of the assets upon which the capital-stock tax is to be assessed, there should be deducted from the market value of the total admitted assets the following amounts: (1) The debt liabilities, and (2) the legal reserves.

As a practicable matter the Unit may have considerable difficulty in distinguishing between the *debt* liabilities, the *reserve* funds, and the *surplus* of an insurance company. The reserve funds of a life insurance company ordinarily include only the net reserve (item No. 7),[1] the reserve to provide for accident and disability benefits in life policies (item No. 8), and the supplementary contract reserve (item No. 9). The debt liabilities include, among other items, the present value of amounts incurred but not yet due for total and permanent disability benefits, liabilities on policies canceled upon which a surrender value may be demanded, total policy claims, dividends left with the company to accumulate at interest, and amounts held to pay commissions, salaries, taxes, etc. (items Nos. 10–33, inclusive, and such portion of item No. 34 as is de-

[1] The item numbers referred to in this paragraph are those contained on page 5 of the annual statement, convention edition, now used in reporting to the State insurance department or commissioner.

clared unconditionally). The items shown in the liabilities statement of insurance companies consisting of amounts held to pay future dividends on annual and deferred dividend policies, held for security fluctuations and general contingency funds, annual dividend equalization funds, etc., constitute surplus or contingent reserves maintained for the general use of the business or reserves the net additions to which are not deductible from gross income in income tax returns (such as items Nos. 35, 36, 37, 47, 48, and such portion of item No. 34 as is not considered debt liabilities). Therefore, the amount of such surplus or reserves must be held to constitute a part of the capital stock of the company which is liable to the capital-stock tax. Whether the miscellaneous credit items Nos. 38 to 46, inclusive, will be considered legal reserves, debt liabilities, or taxable surplus will depend entirely on the nature of the credit accounts entered under these numbers.

III

The companies contend that the four funds named below should be deducted from the total assets in determining the amount of assets subject to the capital-stock tax: (1) Dividends declared on or apportioned to annual dividend policies; (2) dividends declared on or apportioned to deferred dividend policies; (3) dividends or other profits due policyholders, including those contingent on payment of outstanding and deferred premiums; (4) amounts set apart, apportioned, provisionally ascertained, calculated, declared, or held awaiting apportionment upon deferred dividend policies.

Except as indicated in the next succeeding paragraph, the companies' contention relative to these four funds must be denied. The net additions to these funds are not deducted from gross income in income tax returns. They are, therefore, surplus or reserves "the net additions to which are included in net income under the provisions of Title II" of the Revenue Act of 1918.

Most insurance companies set up on the liabilities side of their ledgers, either as a separate item or included in other items, an amount representing dividends which have been declared unconditionally; these dividends are due and payable * as of the close of the accounting period specified in section 1000 (c) of the Revenue Act of 1918. It is the opinion of this office that dividends so declared and so due and payable are deductible in determining the amount of assets upon which the capital-stock tax is to be imposed.

IV

It appears that it was expressly provided in the original charter of the N Company, granted in ——, that the business should be conducted upon the mutual plan and that all the surplus earnings and undivided profits over and above the dividends on the stock, losses, and expenses are and always have been accumulated and held for the benefit of the

* Counsel for the Government in the instant case construe this as we are informed it was construed by the Bureau, to relate to dividends which were payable before the end of the year for which the statement was made. This might relate to item 34, but it would not apply to item 35 or 36. (R. 94.) The case discussed by the Solicitor in this opinion was one in which company declared the dividend in the middle of the calendar year, and the dividend was payable before the end of the calendar year for which the statement was made.

policyholders. No surplus or undivided profits are distributed to the stockholders. Dividends on the stock are limited to 3½ per cent semiannually, and the taxpayer claims that the corporation, because it "transacts business on the mutual plan, is not required by section 407 of Title IV of the Act approved September 8, 1916, * * * to make the return called for by the Exhibit A, B, and C of Form 707."

* * * * *

From the statement of facts it appears that the control of the N Company has passed into the hands of the policyholders. The basis of its organization is mutuality, and it has been consistently referred to in various court decisions as a mutual insurance company.

There are a great many stock life insurance companies which transact business upon a mutual plan. Whether an insurance company should be classed as a stock company or a mutual company must depend upon the ultimate control of the affairs of the company. If the policyholders are in control, the basis of the organization is mutuality, and it should be classed as a mutual insurance company. If, on the other hand, the stockholders are in control, it should be classed as a stock company. This is a practicable rule which can be easily administered.

Solicitor's Opinion 101 and Law Opinion 1078 are superseded; Solicitor's Opinion 40 so far as inconsistent herewith is revoked.

CARL A. MAPES,
Solicitor of Internal Revenue.

Approved.

D. H. BLAIR,
Commissioner of Internal Revenue.

APPENDIX E

EXTRACTS FROM INSURANCE LAW OF NEW YORK, CONSOLIDATED LAWS OF NEW YORK, CHAP. 33, IN EFFECT 1916-1920 (McKINNEY'S CONSOLIDATED LAWS OF NEW YORK, BOOK 27)

§ 21. *When corporation to be deemed insolvent.*—Every insurance corporation specified in articles two, three, four, and five of this chapter, whose assets and credits are not sufficient to reinsure its outstanding risks in a solvent insurance corporation, shall be deemed insolvent and may be proceeded against as an insolvent corporation.

§ 43. *Impaired mutual insurance corporations.*—If it appears to the superintendent from an examination made by him or by an examiner appointed by him that the assets or capital of any mutual insurance corporation are insufficient to justify its continuance in business, he shall determine the amount of such deficiency and issue a written requisition to the officers of the corporation requiring them to make it good within a time to be specified therein, not less than thirty nor more than ninety days from the service of such requisiton. * * *

§ 82. *When receiver shall not be appointed, or new policies issued.*—No receiver for any life insurance corporation shall be appointed if such corporation has actual funds invested according to law, of a net cash value equal to its outstanding liabilities, exclusive of any contingent liability incurred under the provisions of section seventy-one of this chapter relating to the organization of a mutual corporation, and a sufficient reserve on policies and claims not matured, calculated according to the American experience table of mortality,

with interest at four and one-half per centum per annum, and in computing such liabilities, capital stock shall be considered as a liability of the corporation. But no such corporation shall issue new policies if its capital stock is impaired to the extent of fifty per centum thereof, after charging said corporation with a reserve liability calculated according to the provisions of section eighty-four of this chapter, until such impairment is made good; in the case of a corporation having no capital stock, it shall not issue new policies if its assets are less than its liabilities as above defined and upon the basis last before mentioned, until such deficiency is made good.

§ 83. *Distribution of surplus to policyholders.*— Except as herein provided, every domestic life insurance corporation heretofore or hereafter organized, whether incorporated by special act or under a general statute, anything in its charter or certificate of incorporation or in such special act or general statute to the contrary notwithstanding, shall provide in every policy issued on or after the first day of January, nineteen hundred and seven, that the proportion of the surplus accruing upon said policy shall be ascertained and distributed annually and not otherwise. Upon the thirty-first day of December of each year, or as soon thereafter as may be practicable, every such corporation shall well and truly ascertain the surplus earned by such corporation during said year. After setting aside from such surplus such sums as may be required for the payment of authorized dividends upon the capital stock, if any, and such sums as may properly be held for account of existing deferred dividend policies and for a contingency reserve not in excess of the amount prescribed in this article,

every such corporation shall apportion the remaining surplus equitably to all other policies entitled to share therein. * * *

§ 86. *Assets and liabilities of life and casualty insurance corporations; method of computation; procedure in case of impairment; reserve.*—1. In estimating the condition of any life insurance corporation, under the provisions of this chapter, or in any examination made by him, or by an examiner appointed by him, the superintendent shall allow as assets only such investments as are authorized by the laws of this state, and shall charge as liabilities, in addition to the capital stock, all outstanding indebtedness of the corporation, and the premium reserve on policies, and additions thereto in force computed according to the table of mortality and rate of interest prescribed in this article. * * *

§ 87. *Contingency reserve.*—Any domestic life-insurance corporation may accumulate and maintain in addition to an amount equal to the net values of its policies computed according to the standard adopted by it under section eighty-four of this chapter a contingency reserve not exceeding the following respective percentages of said net values, to wit: When said net values are less than one hundred thousand dollars, twenty per centum thereof or the sum of ten thousand dollars, whichever is the greater; when said net values are greater than one hundred thousand dollars, the percentage thereof measuring the contingency reserve shall decrease one-half of one per centum for each one hundred thousand dollars of said net values up to one million dollars; one-half of one per centum for each additional one million dollars up to ten mil-

lion dollars; one-half of one per centum for each additional two million five hundred thousand dollars up to fifteen million dollars; and if said net values equal or exceed the last-mentioned amount, the contingency reserve shall not exceed ten per centum thereof; provided that as the net values of said policies increase and the maximum percentage measuring the contingency reserve decreases such corporation may maintain the contingency reserve already accumulated hereunder; although for the time being it may exceed the maximum percentage herein prescribed, but may not add to the contingency reserve when the addition will bring it beyond the maximum percentage. Provided, however, that nothing herein contained shall be construed to affect any existing surplus or contingency reserves held by any such corporation save that whenever the existing surplus and contingency reserves, exclusive of said net values and of all accumulations held on account of existing deferred dividend policies or groups of such policies, shall exceed the limit above mentioned it shall not be entitled to maintain any additional contingency reserve. Provided further, that for cause shown, the superintendent of insurance may at any time and from time to time permit any corporation to accumulate and maintain a contingency reserve in excess of the limit above mentioned for a prescribed period, not exceeding one year under any one permission, by filing in his office a decision stating his reasons therefor and causing the same to be published in his next annual report. This section shall not apply to any corporation doing exclusively a nonparticipating business. (As amended by Laws of 1920, c. 420.)

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